



BEFORE THE ARIZONA CORPORATION COMMISSION

ROBERT "BOB" BURNS

Chairman

BOYD DUNN

Commissioner

SANDRA D. KENNEDY

Commissioner

JUSTIN OLSON

Commissioner

LEA MARQUEZ PETERSON

Commissioner

Arizona Corporation Commission

DOCKETED

JUN 27 2019

DOCKETED BY

aa

IN THE MATTER OF THE RATE REVIEW
AND EXAMINATION OF THE BOOKS
AND RECORDS OF ARIZONA PUBLIC
SERVICE COMPANY AND ITS
AFFILIATES, SUBSIDIARIES AND
PINNACLE WEST CAPITAL
CORPORATION.

DOCKET NO. E-01345A-19-0003

DECISION NO. 77270

ORDER

Open Meeting
June 11-12, 2019
Phoenix, Arizona

BY THE COMMISSION:

FINDINGS OF FACT

Introduction.

1. Arizona Public Service Company ("APS" or "Company") is certificated to provide electric service as a public utility in Arizona.

2. On January 9, 2019, the Arizona Corporation Commission ("Commission"), consistent with the letter filed by Chairman Burns and Commissioner Dunn on December 24, 2018, directed the Utilities Division Staff ("Staff") to conduct a review of the effectiveness of APS's Customer Education and Outreach Program ("CEOP") utilized in the Company's last rate case. The Commission also directed Staff to initiate a rate review of APS's current rates in order to determine whether APS is over-earning, utilizing a 2018 test year.

3. A rate review is intended to provide a snapshot of the Company's financial position or earnings at any given point in time. It differs from a rate case in that it is for informational purposes only and is not intended to result in any change in the Company's rates. It is used to

1 inform the Commission whether a rate case is necessary. By contrast a rate case for a Class A
2 Utility such as APS typically takes twelve months; whereas a rate review is completed in
3 considerably less time. The additional time for a rate case is required to accommodate the more
4 in-depth evaluation of the issues and the requirements of R14-2-103.

5 4. On February 11, 2019, Staff issued a Request for Proposal ("RFP") related to the
6 APS rate review to 147 consulting companies. The RFP was also posted to the Commission's
7 website. On February 25, 2019, Staff received two responses to the RFP. Ultimately, Staff
8 selected Overland Consulting to assist it in performing the rate review audit which consisted of a
9 review of APS's rate base, cost of capital, adjustors and rate design.

10 5. Staff, in conjunction with Overland Consulting, filed the Report requested by the
11 Commission on June 4, 2019. The Report contains findings and recommendations on the
12 effectiveness of the CEOP and the results of the review of APS's rate base, cost of capital,
13 adjustors and rate design.

14 6. As a result of the Report's findings. Staff is recommending that APS file a rate case
15 by October 31, 2019 utilizing a test year ending June 30, 2019.

16 **Background.**

17 7. APS, a subsidiary of Pinnacle West Corporation ("Pinnacle West"), is the largest
18 provider of electric service in Arizona, and at the time of APS's last rate case served more than 1.2
19 million customers in 11 of Arizona's 15 counties.

20 8. APS's last rate case was filed in 2016 and utilized a 2015 test year. Decision
21 No. 76295 was issued on August 18, 2017, which in addition to authorizing a net base rate increase
22 of \$94.62 million, approved modernized rate plans that deviated significantly in some respects
23 from prior rate plans.

24 9. APS and the Commission received numerous complaints regarding rate increase
25 notices, customers' lack of understanding of the modernized rate designs, and concerns about
26 being placed on demand rates.

27 ...

28 ...

Overview of Report Findings.*A. Customer Education and Outreach Program.*

10. The review of APS's CEOP looked at: (1) the CEOP's methods, procedures, customer reach, and the understandability of information provided; (2) the effectiveness of the CEOP in meeting the objective of providing customers with complete and accurate information about the rate increase and rate plan changes approved in the Decision including the information needed to enable customers to make informed rate plan selections; and that customers could experience varying results based upon individual circumstances; (3) whether the CEOP expenditures were reasonable, incremental in that they would not have been made absent the CEOP, and directly associated with the CEOP.

CEOP Methods, Procedures and Customer Reach

11. With respect to the first criteria, the majority of the information communicated to customers in APS's CEOP was not reasonable and understandable. Some of the most important information was conveyed in personalized letters that described the new rate plans, and in particular the new rate plans "most like" customers' existing rate plans, and the rate plans likely to be "most economical" given customers' recent historical usage.

12. The scope of the CEOP was adequate to reach APS's entire residential customer base. However, there were notable exceptions:

- APS did not have email addresses for approximately 45% of its residential customer base in early 2018.
- Radio and billboard advertising related to the CEOP was confined to the Phoenix metro area.
- The following were only provided in English: (1) emails, (2) aps.com transactional pages, (3) aps.com banner ads and pop-ups, (4) IVR-based plan assistance, (5) special interest letters (6) mass media campaigns, (7) notifications, (8) service plan comparison tool, and (9) peak demand calculator.

- APS can only send marketing emails (used to drive awareness of and participation in customer programs) to customers who have agreed to receive email communications.

13. As part of the CEOP, APS created several tools to help customers select new rate plans and to manage their electricity usage. The most important of these was a rate comparison tool launched on the APS website that enabled customers to compare projected annual costs under their existing legacy rate plans to those associated with new rate plans. Customer dissatisfaction caused by higher bills and the new modernized rate plans may have been worse had the rate comparison tool not been available.

14. APS's CEOP should have included more personal customer contact or outreach efforts regarding the new modernized rate plans and which plan would be of most benefit to the customer.

15. APS did not provide an explanation of adjustor mechanisms in its CEOP, nor did APS clarify the fact that there would be annual updates to the adjustor mechanism billing rates occurring outside of the rate case and that such rate changes may result in an increase in customer bills. These additional bill adjustments may have been confusing to some customers, especially if APS did not give notice of the adjustor changes.

CEOP Effectiveness – Non-Solar Customers

16. To determine how effective the CEOP was, a sample of customer complaints were analyzed. The analysis of 2018 customer complaints classified by APS as "rate case" related showed the following:

- Some customers complained that the 4.5%/\$6 per month average rate increase advertised by APS in 2017 understated the actual increase.
- Some customers perceived that the rate plan transition that occurred in spring 2018, which followed the rate increase under legacy rate plans in 2017, amounted to a second increase in their utility rates.

...

...

- Some customers may have been dissatisfied with being moved to new, sometimes differently structured rate plans, and rate plans with different peak hours, then previous rate plans.
- Some customers moved to new rate plans may have experienced or perceived that the rate plans caused significant increases in their bills.
- Some customers were unhappy with being placed on rate plans with a demand component.

17. The information provided by APS in its rate increase notices and personalized letters failed to convey certain important information, including:

- The “average customer” rate increase percentage and bill impact (4.5% increase, \$6 per month) disclosed in customer notices and press releases failed to adequately convey that the impact of the modernized rate design on individual customers could vary widely, and over time, depending on customer-specific circumstances and changes in other customer bill components such as adjustors and taxes and fees, and were not included in the notice regarding the average percentage or bill increase.
- The rate plan transition letters mailed in the first few months of 2018 failed to adequately convey to customers additional increases in their bills, beyond those that occurred with the 2017 transition rates. The information conveyed did not include that these additional increases in bills were dependent on customer-specific circumstances, including the specific rate plans that customers were on before and after the transition, and behavioral changes in energy usage patterns under the new rate plans which could minimize bill increases, such as shifting usage to accommodate the new on-peak hours and demand charges.

CEOP Effectiveness – Solar Customers

18. APS’s CEOP messaging did not inform solar customers or applicants of the August 31, 2017 deadline for changing their legacy rate plans or the potential advantages of doing so.

1 19. Solar customer complaints show that existing customers and applicants were
2 sometimes unaware of the potential advantages and disadvantages of different legacy rate plans
3 under net metering because they believed that nothing was required of them to take full advantage
4 of the net metering rules.

5 20. APS's rate comparison tool did not incorporate legacy rate plans or retail net
6 metering, which, had it been available before the August 31, 2017 deadline, would have permitted
7 solar customers to assess the benefits of different rate plans under net metering.

8 21. Although August 31, 2017 was the stated deadline for solar customers and
9 applicants to change their legacy rate plan, there are examples in which APS made exceptions,
10 allowing customers to change rate plans after the deadline.

11 CEOP Expenditures

12 23. Of the \$5 million authorized, APS expended \$4.85 million on the CEOP between
13 September 2017 and February 2019. Outside (vendor) materials and services accounted for \$4.28
14 million (88%), and \$474,000 (10%) was primarily internally-incurred print shop costs, with the
15 remaining \$94,000 (2%) associated with payment for contract and APS employees who charged
16 time to CEOP projects.

17 24. Overall, CEOP expenses incurred between September 2017 and February 2019
18 were reasonable, directly related to CEOP activities, and incremental to the CEOP work.

19 25. The expenses associated with the three largest CEOP vendors accounted for 62% of
20 total CEOP vendor costs and were directly applicable to CEOP efforts and services. These costs
21 were properly incurred and incremental to the CEOP and appropriate within the scope of the
22 CEOP.

23 26. Internal cost allocations and transfers charged to CEOP were appropriate.

24 *B. Billing Determinants and Rate Design*

25 27. Although APS's 2018 base retail residential revenues were aligned with 2015
26 estimates overall, the number of medium- and large-usage customers transitioning to demand rates
27 did not meet Company expectations. The comparison of typical bills shows that customers on
28 demand rates were expected to see smaller overall bill increases, and actual bill savings if

1 converting from a basic rate plan. As a result, should these customers continue on sub-optimal rate
2 plans, APS could see higher than anticipated revenues in future years.

3 28. The design of the Company's new rate plans may have incentivized the selection of
4 demand rates over basic rates and energy rates. The analysis of typical bills indicates that rate
5 increases for basic (one-part) and time-of use energy (two-part) rate plans were higher than
6 average, while demand (three-part) rate plans had lower than average increases. Furthermore,
7 customers who were moved by APS onto a rate plan "most like" their previous rate plan were less
8 likely to be on the most economical rate plan.

9 29. \$6.7 million of gross margin in 2018 was associated with higher than expected
10 revenues due to variances between the assumptions in the billing determinants utilized in the 2016
11 rate case and actual 2018 billing determinants.

12 *C. Rate Review*

13 The Report identifies the following important changes since the 2016 rate case, all of
14 which support Staff's recommendation that a new rate case be filed sooner than later.

15 30. There have been significant departures from the Company's projected 2015
16 customer billing determinants to the actual customer billing determinants occurring in 2018.

17 31. There has been noteworthy customer growth in APS's customer base; APS has that
18 residential accounts have increased at a 1.7% annual rate since 2015. Due to this increase in
19 customer base, APS's revenue for 2018 compared to 2017 may have increased.

20 32. There has been substantial investment in plant and infrastructure that may have
21 increased the Company's rate base.

22 33. The impact of pro forma adjustments in a rate case will impact both revenues and
23 expenses. These adjustments could include weather normalization, plant additions, interest
24 synchronization and income tax expense normalization. APS did not include any pro forma
25 adjustments in the 2018 actual data.

26 34. According to a recent Earnings Call, the Company is actively managing costs, and
27 identifying additional efficiencies and savings throughout the organization.
28

35. According to APS, the current embedded cost of debt is 4.19%. This represents a decrease from 5.13% in the 2016 rate case.

36. Based on current market conditions and interest rates, as compared to 2016, there is a possibility of changes to the cost of equity. In addition, according to APS, the new capital structure target is an equity ratio between 53.8% and 55.8%.

37. A 0.8% return on the fair value increment was approved in Decision No. 76295. However, the Commission may desire to reexamine this issue in the next rate case.

38. A review of all of the adjustor mechanisms in a rate case, may lead to potential modifications.

Staff Recommendations.

A. CEOP

39. It is reasonable to have APS fund and implement a Customer Outreach and Education Program to be developed and administered by Commission Staff. Therefore, it is recommended that Staff select and hire an independent consultant, paid for by APS, to develop a program to properly and adequately educate customers on all aspects of APS's rate plans.

40. It is in the public interest for APS to provide customers with pro forma billing information on how much they would owe, given their actual usage during each month, if the customer was on his/her most economical plan. In addition to providing pro forma billing for each period on an ongoing basis, the Company shall also provide the pro forma billing for each customer who is not currently on their most economical plan for each billing period during the last 12 months. The Company shall continue to provide this billing information until the conclusion of the Company's next rate case or upon further order of the Commission.

41. In future rate cases, APS should thoroughly explain and quantify the impact of adjustor mechanisms on rates.

42. It is reasonable for APS to fund and organize along with the assistance of an independent third-party consultant, a stakeholder group to collaborate and suggest better ways to communicate the impact of changes and adjustor mechanisms to residential customers, including more effective ways to educate customers on rate plans and ways to cut back on energy usage.

1 43. It is reasonable for APS to allow an additional opportunity for customers to switch
2 rate plans for at least a four-month enrollment period during which customers should be allowed to
3 select a different rate plan. We agree with Staff that customers should be allowed an additional
4 opportunity to switch rate plans, however, we believe the enrollment period should be for six (6)
5 months instead of four (4) months.

6 44. APS should identify ratepayers whose bills have increased by more than 9 percent
7 under the new rate plans, based on 2015 Test Year determinants, and those ratepayers who are not
8 on their most economical plans, and provide the ratepayers most impacted with targeted
9 educational materials that explain: (1) the various rate plans; (2) the various options available, (3)
10 comparative usage data for their current plan and their most economical plan; and (4) the
11 opportunity to switch plans.

12 45. It is reasonable for APS to prepare and Staff to use a “bin-analysis” to provide more
13 meaningful notice of estimated bill impacts to customers.

14 46. APS should provide grandfathered net metered solar customers with legacy demand
15 rates (ECT-1R EPR and ECT-2-EPR) an additional opportunity to switch to a rate plan that
16 enables them to fully benefit from net metering (E12, ET-1 or ET-2). APS should provide notice
17 to these customers to ensure they are made aware of the opportunity to switch to a more
18 advantageous legacy rate plan. In addition, APS should provide educational materials to these
19 customers about the advantages and disadvantages of each legacy rate plan that can be paired with
20 solar net metering. The window of opportunity to switch rate plans should remain open for a
21 reasonable time (e.g., the remainder of 2019) to ensure that all remaining demand rate solar
22 customers have either transitioned to another legacy rate plan or positively confirmed for APS
23 that they wish to remain on their existing demand rate.

24 47. APS shall also track and report, in this docket, to the Commission, on a quarterly
25 basis the status of the Customer Education and Outreach Program, including stakeholder
26 engagement efforts, customer plan selection, and any changes in usage patterns for customers
27 since the implementation of the new rate plans.

1 *B. Billing Determinants and Rate Design*

2 48. Given the risk of variances in the distribution of customers on the various
3 residential rate plans from those assumed in the 2016 rate case, APS should prepare a metric to
4 track the progress of customer rate plan conversions as compared against the assumed rate case
5 filing determinants.

6 49. APS should provide updated excess earnings data through June 2019 associated
7 with higher than expected revenues due to changes into modernized rate designs made in the 2016
8 rate case.

9 50. APS shall track and report, in this docket, to the Commission, on a quarterly basis
10 the amount of gross margins associated with the higher than projected revenues due to the
11 variances between the assumptions in the billing determinants utilized in the 2016 rate case and
12 actual 2018 billing determinants.

13 *C. Rate Review.*

14 51. Due to the changing factors discussed in the Report, including APS's investment in
15 plant and infrastructure that may have increased rate base, changes in revenues and expenses, the
16 potential reduction in operations and maintenance expenses, possible changes to APS's cost of
17 capital, and its customer base growth and billing determinants (modernized rates), which are some
18 key components of the rate-making process, it is appropriate for APS to file a new rate case to
19 reflect these changes. Therefore, it is Staff's recommendation that APS be required to file a rate
20 case no later than October 31, 2019, utilizing a 12-month test-year period ending June 30, 2019.
21 Thereafter, the Commission, based on its rate-making authority, will determine the just and
22 reasonable rates for APS, ratepayers and stakeholders.

23 **CONCLUSIONS OF LAW**

24 1. APS is an Arizona public service corporation within the meaning of Article XV,
25 Section 2 of the Arizona Constitution.

26 2. The Commission has jurisdiction over APS and over the subject matter of the Rate
27 Review Report submitted by Staff on June 4, 2019.
28

3. The Commission, having reviewed Staff's Rate Review Report concludes that the findings and recommendations contained therein are reasonable and that it is in the public interest to adopt the recommendations contained therein.

ORDER

IT IS THEREFORE ORDERED that the findings contained in the Utilities Division Staff's Rate Review Report are reasonable and in the public interest and are hereby adopted.

IT IS FURTHER ORDERED that Findings of Facts 39 through 51 herein containing Staff's recommendations, and as modified by the Commission, are reasonable and in the public interest and are hereby adopted.

IT IS FURTHER ORDERED that Arizona Public Service Company shall file a rate case no later than October 31, 2019, utilizing a 12-month test-year period ending June 30, 2019. Arizona Public Service shall also file its 2017 expenditures as a supplemental report.

...

...

...

...

...

...

...

...

...

...

...

...

...

...

...

...

IT IS FURTHER ORDERED that this Decision shall be effective immediately.

BY THE ORDER OF THE ARIZONA CORPORATION COMMISSION


CHAIRMAN BURNS


COMMISSIONER DUNN


COMMISSIONER KENNEDY


COMMISSIONER OLSON


COMMISSIONER MARQUEZ PETERSON

IN WITNESS WHEREOF, I, MATTHEW J. NEUBERT,
Executive Director of the Arizona Corporation Commission,
have hereunto, set my hand and caused the official seal of
this Commission to be affixed at the Capitol, in the City of
Phoenix, this 27 day of
June 2019.




MATTHEW J. NEUBERT
EXECUTIVE DIRECTOR

DISSENT: _____

DISSENT: _____

EOA:CLA:elr/MAS

SERVICE LIST FOR: ARIZONA PUBLIC SERVICE COMPANY
DOCKET NO. E-01345A-19-0003

Stacey Champion
3101 N. Central Ave, Suite 174
Phoenix, AZ 85012
sc.@champion-pr.com

Consented to Service by Email

Thomas Mumaw
Pinnacle West Capital Corporation
400 N. 5th Street, MS 8695
Phoenix, Arizona 85004
Thomas.Mumaw@pinnaclewest.com
Kerri.Carnes@aps.com
Melissa.Krueger@pinnaclewest.com
Thersea.Dwyer@pinnaclewest.com
Debra.Orr@aps.com

Consented to Service by Email

Robin R. Mitchell
ARIZONA CORPORATION COMMISSION
Director - Legal Division
1200 W. Washington St.
Phoenix, AZ 85007
LegalDiv@azcc.gov
utildivservicebyemail@azcc.gov
Consented to Service by Email